

REPORT OF THE EXECUTIVE OFFICER
State Allocation Board Meeting, May 28, 2008

FINANCIAL HARDSHIP PROGRAM REGULATORY AMENDMENTS

PURPOSE OF REPORT

To request:

1. Adoption of proposed regulatory amendments to the Financial Hardship (FH) Program.
2. Authorization to file the proposed regulations with the Office of Administrative Law (OAL) on an emergency basis.

BACKGROUND

At the April 23, 2008 State Allocation Board (SAB) meeting, the SAB requested the Office of Public School Construction (OPSC) to bring back to the May 28, 2008 meeting proposed regulatory amendments to the FH Program. Revisions were requested due to issues disclosed from OPSC's recent FH reviews.

Staff met with representatives from County Offices of Education on May 9, 2008 and the FH Advisory Group on May 12, 2008 to discuss broad concepts for reforming FH. Meeting participants discussed program integrity and program improvement concepts. These concepts were then incorporated into draft regulations that were presented at the May 16, 2008 Implementation Committee meeting. Some Implementation Committee members expressed concern that the regulation changes were too broad to consider in one meeting. After a lengthy discussion, Staff committed to scaling back the regulations for consideration at the May SAB with a commitment from stakeholders to bring forward broad FH reforms to the July SAB. Staff used this discussion, along with other suggestions intended to help improve the FH program, to create the proposed regulations that are being presented for adoption today. Staff will continue to meet and work with school districts, county offices of education, practitioners, the FH Advisory Committee and the Implementation Committee to present more extensive reforms to the July 2008 SAB meeting.

AUTHORITY

Education Code Section 17075.15 and the School Facility Program (SFP) Regulation Section 1859.81 outline the requirements of the FH program

STAFF COMMENTS

The OPSC has drafted proposed regulation changes for the FH Program (attached). These regulatory changes will improve program integrity, clarity, and uniformity. The following concepts summarize the proposed regulatory changes:

1. REQUIREMENTS FOR THE PROGRAM

All districts must fully disclose all financial information and resources for capital facilities funding. In addition, the district must create and maintain within Fund 35 (Capital School Facilities Fund as defined by the California Department of Education (CDE) School Accounting Manual) a sub-fund account or unique account code for each SAB SFP project. All SFP project revenues and expenditures will be accounted for in this fund. This accounting practice, already adopted by most districts, will provide more uniformity and accountability over State bond funds. Failure to meet these conditions will result in termination of the district's FH status.

(Continued on Page Two)

STAFF COMMENTS (cont.)

2. REVIEW PROCESS

These proposed changes to the FH review process create uniformity and clarity in the review process. First, FH eligibility for the program will be determined. Second, the district's available funds will be determined. The district will first submit evidence it meets FH eligibility requirements. If OPSC determines a district is eligible for FH, the OPSC will notify the district of its eligibility and request documentation to determine the district's contribution.

Proposed changes clarify the reporting requirements and time-frame for the determination of district contribution. Within 30 days of notification, the district must clearly identify any available funds it can contribute as matching share and submit complete documentation to confirm funds. The documentation can be no older than 30 days prior to the district's submission of documentation. Revenues must include all capital facility funding designated for capital outlay purposes, current and accrued. Accrued revenues are defined as revenues that will be received within six months of district documentation submission date, including apportioned State grants. For SFP projects, encumbrances will not be allowed for the State's share of the liability. Additionally, if the review of available funds has not concluded within 60 days from receipt of complete documentation by the OPSC, the district will be required to submit a one-time update of documentation of their available funds.

These proposed changes will ensure that the determination of district contribution is made on current and timely information. In addition, accrued revenue to be received within six months of the complete documentation submission date will now be included as part of district contribution.

Currently, program integrity is considered compromised. These regulations establish clear rules on the review process, provide clear rules on accounting for SFP funds, and provide limited relief to program integrity issues. Broader reforms, however, are still essential and will be coming forward at the July 2008 SAB meeting.

RECOMMENDATIONS

1. Adopt the proposed regulations as shown on the Attachment.
2. Authorize Staff to begin the regulatory process with the OAL on an emergency basis.

BOARD ACTION

In considering this item, the State Allocation Board requested that this issue be returned to the Implementation Committee for further discussion and requested staff to report back at a future SAB meeting. The Board requested that the following issues be addressed and/or explored:

- How are district encumbrances being accounted for and reported?
- Define "accrued revenue" and further define "State encumbrance."
- Ensure that the apportioned State grants are reflected in district revenue.
- What is a complete application as determined by the OPSC?
- What types of projects are Financial Hardship districts building?
- How does Financial Hardship impact County Offices of Education?

Amend Regulation Section 1859.81

Section 1859.81. Financial Hardship.

As a condition of receiving FH status and funding approval, all districts shall:

- (a) Fully disclose all financial information and resources for capital facilities funding.
- (b) Follow the CDE California School Accounting Manual and create and maintain a sub-fund account or unique account code for each SAB SFP project within Fund 35 (Capital School Facilities Fund) for all revenues and expenditures including, but not limited to, SFP grants and school district contributions.

Failure to meet the above conditions will result in the termination of the district's FH status. Upon proof of compliance with above conditions, satisfactory to the OPSC, districts may reapply for FH status.

Except for Joint-Use Projects and Career Technical Educational Facilities Projects, a district is eligible for financial hardship to fund all or a portion of its matching share requirement after demonstrating the requirements of (a), ~~(c), (d),~~ through (f), below:

- (c) The district has made all reasonable efforts to fund its matching share of the project by demonstrating it is levying the developer fee justified under law or an alternative revenue source equal to or greater than the developer fee otherwise justified under law at the time of request for hardship and the district meets at least one of the following:
 - (1) The current outstanding bonded indebtedness of the district issued for the purpose of constructing school facilities in accordance with Education Code Section 17072.35 or 17074.25 as appropriate, at the time of request for financial hardship status, is at least 60 percent of the district's total bonding capacity. Outstanding bonded indebtedness includes that part of general obligation bonds, Mello-Roos Bonds, School Facility Improvement District Bonds and certificates of participation which the district is paying a debt service that was issued for capital outlay school facility purposes.
 - (2) The district had a successful registered voter bond election for at least the maximum amount allowed under Proposition 39 within the previous two years from the date of request for financial hardship status. The proceeds from the bond election that represent the maximum amount allowed under the provisions of Proposition 39 must be used to fund the district's matching share requirement for SFP project(s).
 - (3) It is a County Superintendent of Schools.
 - (4) The district's total bonding capacity at the time of the request for financial hardship status is \$5 million or less.
 - (5) Other evidence of reasonable effort as approved by the SAB.

If the district's request for financial hardship status is denied by the Board, the district may be deemed eligible for rental payments of \$2,000 per year per classroom under the Emergency School Classroom Law of 1979 for a two year period when relocatable classroom buildings are available and the district provides financial documentation that it is unable to afford the full rental amount and any other information satisfactory to the Board that the rental reduction is necessary. The number of classrooms eligible for the \$2,000 rental payments shall be the sum of the numbers determined in (c)(5)(B) as follows:

- (A) Determine the number of pupils by grade level that the district requested a New Construction Grant on the Form SAB 50-04 that were denied financial hardship status.
- (B) Divide the number by grade level determined in (c)(5)(A) by 25 for K-6, 27 for 7-12, 13 for Non-Severe and 9 for Severe and round up to the nearest whole number.

- (a)(d) Review – The district's review shows that it is financially unable to provide all necessary matching funds for an eligible project. To determine verify this, an analysis the a review shall be made of the district's financial records by the OPSC including data and records maintained by the CDE and the County Office of Education and the school district's latest Independent Audit Reports.
- (1) The analysis shall consist of a review. The district will submit evidence that the district meets the eligibility requirements, as defined in subsection (c), to OPSC.
- (2) If OPSC determines that the district is eligible for FH, OPSC will notify the district of its FH eligibility.
- (3) Within 30 days of notification, an eligible district must clearly identify any available funds it can contribute as matching share and submit complete documentation, as determined by OPSC, to confirm available funds. The documentation can be no older than 30 days prior to the district's submission of documentation and must identify the following:
- (i) Revenues –of the district's latest Independent Audit regarding funds available from all capital facility funding that is designated for capital outlay purposes must include current and accrued revenues. Accrued revenues are those revenues that will be received within 6 months of the documentation submission date accounts, including, but not limited to, apportioned state grants, developer fees, funds generated from capital facility certificates of participation, federal grants, redevelopment funds, sale proceeds from surplus property, the appraised value of facilities approved for replacement pursuant to Section 1859.82, bond funds either encumbered, unencumbered or authorized but unsold, and savings from other SFP projects. All funds thus identified that have not been expended or encumbered by a contractual agreement for a specific capital outlay purpose prior to the initial request for financial hardship status shall be deemed available as a matching contribution.
- (ii) For SFP projects, encumbrances will not be allowed for the state's share of the liability.
- (iii) If the review of available funds has not concluded within 60 days from receipt of complete documentation by OPSC, the district will be required to submit a one-time update of documentation.

Once OPSC determines any available funds the district can contribute as matching share and the district concurs, the 180 day FH status commences. Upon expiration of the 180 day FH status, the district may apply for a renewal review.

(e) A renewal review will be conducted as described in (d) above. After the initial request for financial hardship status is granted, no further. No additional encumbrances will be approved by the OPSC at a renewal review and all prospective capital facility revenue made available to the district's capital facility accounts shall be deemed available as matching contribution on the subsequent financial hardship review, with the exception of:

- (1) Approved interim housing expenditures.
- (2) Funding to pay for previously recognized multi-year encumbrances approved at the initial financial hardship approval.
- (3) Funding that is transferred into a Special Reserve Fund and is used for the express purpose of the Federal Renovation Program when the amount expended out of that fund does not exceed the maximum Federal Renovation Grant amount.
- (4) Funding that is transferred into a Special Reserve Fund and is used for the express purpose of the School Facilities Needs Assessment Grant Program or Emergency Repair Program when the amount expended out of that fund does not exceed the maximum grant amount apportioned.
- (5) Funding that is transferred into a Special Reserve Fund and is used for the express purpose of the Career Technical Education Facilities Program when the amount expended out of that fund does not exceed the applicant's share of the maximum grant amount apportioned.
- (6) Funding that is transferred into a Special Reserve Fund and used for the express purpose of the Overcrowding Relief Grant when the amount expended out of that fund does not exceed the amount of the site acquisition and design costs of the project and the district has submitted an approved Form SAB 50-11.

- (7) Funding that is used for the express purpose of reimbursing the State a proportionate share of financial hardship received when there has been a transfer of a special education program and title to the facility. In addition, the funding was used within five years of the title transfer.
- (8) Funding to pay for obtaining a structural report pursuant to Section 1859.82 for an approvable and funded seismic mitigation project.
- (9) All other capital facility funding for a period of three years when no subsequent financial hardship request is made during this period, with the exception of the funding identified in (6). The three-year period begins with the date of the most recent financial hardship new construction or modernization adjusted grant funding apportionment.

When Overcrowding Relief Grant funding is set aside pursuant to (6) and the School District has not submitted, or the OPSC has not accepted, a Form SAB 50-04 for an Overcrowding Relief Grant within three years from the date of deposit into the Special Reserve Fund, or the School District has not met the requirements in Sections 1859.90 or 1859.105, remaining funds plus interest accrued at the Pooled Money Investment Board rate at that time period shall be deemed available as matching contribution on a subsequent financial hardship project or be captured through an audit adjustment pursuant to Section 1859.106.

- ~~(d)(f)~~ The district has not signed a contract for acquisition or construction of classrooms that replace existing facility(ies), which were included in the determination of the district's new construction eligibility pursuant to Education Code Section 17071.75, in a locally funded project during the five-year period immediately preceding the district's application for financial hardship assistance. This restriction may be lifted if the Board finds that unforeseen and extenuating circumstances existed that required the district to use local funds to replace the facility(ies).

~~(b)(g)~~ From the funds deemed available as a matching contribution, the district may retain \$19,776 per classroom in each enrollment reporting period for the cost to provide interim housing for the currently unhoused pupils of the district. The amount shown shall be adjusted annually in the manner prescribed in Section 1859.71. The number of classrooms needed for interim housing for the currently unhoused pupils shall be the sum of the positive numbers determined in ~~(b)(g)(7)~~ as follows:

- (1) Determine the current enrollment of the district by grade level as shown on the latest Form SAB 50-01.
- (2) Determine the New Construction Grants apportioned by grade level for all SFP projects and LPP funded under the provisions of Sections 1859.12 or 1859.13 where the district has submitted Form SAB 50-06 indicating that the project is 100 percent complete.
- (3) Subtract ~~(b)(g)(2)~~ from ~~(b)(g)(1)~~.
- (4) Determine the number of classrooms by grade level reported in Part 1, Line 8 on Form SAB 50-02.
- (5) Multiply the classrooms determined in ~~(b)(g)(4)~~ by 25 for K-6, 27 for 7-12, 13 for Non-Severe and 9 for Severe.
- (6) Subtract the product determined in ~~(b)(g)(5)~~ from the difference determined in ~~(b)(g)(3)~~ by grade level.
- (7) Divide the difference by grade level determined in ~~(b)(g)(6)~~ by 25 for K-6, 27 for 7-12, 13 for Non-Severe and 9 for Severe and round up to the nearest whole number.

From the funds deemed available as a matching contribution, the district may also retain \$19,776 per portable toilet unit in each reporting period for the cost to provide necessary interim toilet facilities for the currently unhoused pupils of the district. The amount shown shall be adjusted annually in the manner prescribed in Section 1859.71. The number of toilet facilities needed for interim housing shall be the sum of the positive numbers determined in ~~(b)(g)(7)~~ divided by eight rounded up to the nearest whole number.

If the district's available funds, as determined by the OPSC analysis less costs for interim housing, is less than its matching share, the district will be deemed to have met the requirements of this Subsection.

If the district meets the financial hardship requirements in this Section, the amount of financial hardship is equal to the district's matching share less funds deemed available in ~~(a)~~(d) or (e).

The financial hardship analysis is subject to approval by the Board.

Once a district has been notified by the OPSC that it meets the requirements of financial hardship in this Section, the district may file Form SAB 50-04 under the provisions of financial hardship anytime within a period of 180 calendar days from the date of the OPSC notification. If the district does not submit Form SAB 50-04 under the provisions of financial hardship within 180 calendar days of the OPSC notification of approval of financial hardship status, the district must re-qualify for financial hardship status under the provisions of this Section by submittal of a new request for financial hardship status.

If the district submits Form SAB 50-04 within 180 calendar days of the OPSC notification of approval of financial hardship and the project(s) has been included on an unfunded list for more than 180 calendar days, a review of the district's funds pursuant to ~~(a)~~(d) or (e) will be made to determine if additional district funds are available to fund the district's matching share of the project(s). Financial hardship approval status by the OPSC for a separate design and/or site apportionment does not apply to any subsequent funding for the project(s).

Note: Authority cited: Sections 17070.35, 17075.15, 17078.72 and 17592.73, Education Code.

Reference: Sections 17071.75, 17075.10, 17075.15, and 17079.20, Education Code.